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# **RATE REGULATION:**

**HOW ITS UNINTENDED  
CONSEQUENCES COULD  
GREATLY HARM PROGRAM  
SERVICES**

## CURRENT IMPACT ON DCI DUE TO THREAT OF RATE REGULATION

- TLC LAUNCHES ARE STALLED AS OPERATORS AWAIT RE-REGULATION AND REFUSE TO LAUNCH ANYTHING MORE ON BASIC
- OPERATORS SAY "BASIC IS DEAD" "WE HAVE TO TIER YOU" BECAUSE WE CAN'T PASS ON COSTS IF WE ADD YOU TO BASIC
- AS OPERATORS MAKE ROOM FOR MUST CARRY, THEY USE UP CHANNELS AND CAN'T LAUNCH TLC
- WE HAVE HAD TO DRAMATICALLY SCALE BACK OUR BUSINESS PLAN

EXPECTATIONS FOR TLC COM NOW 20 COM CURE VC COM 2 AN ACCT

# **OUR PASSIONATE PLEA**

**DON'T LET RATE REGULATION HURT  
NEW CHANNELS LIKE LEARNING  
ANY MORE THAN WE'VE BEEN HURT  
ALREADY.**

# WHY BEING ON BASIC IS OPTIMAL

- . Being on basic gives 100% of viewers in any market a chance of seeing your service
- . Because basic carriage maximizes your sub volume, viewership and thus advertising revenue are maximized
- . Consumers benefit: programming fee charged to affiliates, and ultimately consumers, is minimized

## WHY BEING ON A TIER SUB-OPTIMIZES

- In tiered world, subscribership and therefore viewership and ad revenue are limited; perhaps greatly limited
- Subscribership is limited because only a percentage choose to pay the extra fee
- Viewership is limited because there is a smaller pool who can choose to view any given network
- Ad revenue is limited because subscribership and viewership are limited

Marketing costs are greatly increased because of the expense of

## THE ECONOMICS TO A PROGRAMMER OF BEING CARRIED ON BASIC VS. BEING CARRIED ON TIER

### ASSUMPTIONS:

- A network is carried by affiliates servicing 20 million "basic" households.
- Total annual expenditures for the network amount to \$50 million.
- In order to hit financial "break-even", the network must be able to achieve ad plus affiliate revenues totaling \$2.50 per "basic" household ( $\$2.50 \times 20 \text{ million}$ ).
- For every household that the network is in, \$1.25 of ad revenue is expected to be earned (assuming viewership estimates are achieved).

## **OTHER PROBLEMS CAUSED BY TIERS:**

**REDUCTION IN SAMPLING UNIVERSE NEGATIVELY AFFECTS RATINGS.**

**ADVERTISERS WILL PAY US LESS IF THEY GET A "PORTION" OF ALL THE MAJOR MARKETS (20-30%) VERSUS ALL OF THE MAJOR MARKETS.**

**PERCEPTION OF GROWTH AND MOMENTUM IS VITAL TO ADVERTISERS. ON TIERS, GROWTH IS GREATLY SLOWED.**

**TIERS ARE EXTREMELY CONFUSING TO CONSUMERS. MARKETING TENDS TO SOUND LIKE ALPHABET SOUP.**

## PROBLEMS WITH TIERS CONTINUED....

OUR BUSINESS PLANS CANNOT ABSORB THE HIGH COSTS OF THE CONSTANT MARKETING THAT'S NECESSARY.

ADVERTISING IS A MULTI-LEVELED SALE. LOTS OF PEOPLE HAVE TO BELIEVE IN YOUR NETWORK. BUT ADVERTISERS ARE VIEWERS TOO. IF

## ANALYSIS OF AFFILIATE FEE PRICING BASED ON DIFFERENT TIERING LEVEL SCENARIOS:

NETWORK PENETRATION	NETWORK SUBSCRIBERS*	ANNUAL AD SALES (@\$1.25/SUB)	REQUIRED SUB REVENUE (FOR "BREAK-EVEN")	REQUIRED SUBSCRIBER FEE/MONTH
100%	20 MILLION	\$25 MILLION	\$25 MILLION	10.0¢
80%	16 MILLION	\$20 MILLION	\$30 MILLION	16.0¢
60%	12 MILLION	\$15 MILLION	\$35 MILLION	24.0¢
40%	8 MILLION	\$10 MILLION	\$40 MILLION	42.0¢
20%	4 MILLION	\$5 MILLION	\$45 MILLION	94.0¢

\*Out of 20 Million "Basic" Subs

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# RECAP

## **RECAP OF REASONS WHY DISCOVERY COMMUNICATIONS, INC. HAS DIFFERENTIATED IN PRICING TO ITS AFFILIATES**

1. **"CHARTER" AFFILIATES:** THE INITIAL GROUP OF AFFILIATES WHO ASSISTED THE NETWORKS BY AGREEING TO GIVE UP FREE CONTRACTS AND TO PAY A FEE. THEY DESERVE "SPECIAL" PRICING CONSIDERATION.
2. **"VOLUME" DISCOUNTS:** AFFILIATES THAT PROVIDE A GREATER QUANTITY OF SUBSCRIBERS MAKE A GREATER CONTRIBUTION TO NETWORK ADVERTISING AND AFFILIATE REVENUES AND THEREFORE DESERVE SPECIAL PRICING CONSIDERATION
3. **"LOW PENETRATION / TIERING" PENALTIES:** AFFILIATES AND THEIR SYSTEMS THAT PACKAGE OUR NETWORKS IN SUCH A WAY THAT THEY ACHIEVE LOW "PENETRATION" PAY A PENALTY (OR SURCHARGE). THE SURCHARGE IS INTENDED TO RECOVER LOST AD / AFFILIATE REVENUE AND INCENT RE-PACKAGING KEYED TO THE PERCENTAGE OF THEIR SUBSCRIBERS THAT RECEIVE THE SERVICE.
4. **HIGHER COST TO DELIVER, MARKET, OR SERVICE:** IF THERE ARE INCREMENTAL COSTS ASSOCIATED WITH PROVIDING SERVICE TO AN AFFILIATE OR GROUP OF AFFILIATES, THESE COSTS ARE RECOVERED THROUGH A HIGHER RATE PER SUB (E.G. TVRO, TIERS).
5. **STANDARDS/PRACTICES OF NON-VERTICALLY INTEGRATED PROGRAMMERS:** DCI HAS FOLLOWED PRACTICES USED BY NON-VERTICALLY INTEGRATED PROGRAMMERS, I.E., MARKET DRIVEN PRACTICES, BASING ITS TVRO RATE IN PART ON MARKET FACTORS.

**ESTIMATED REVENUE LOSS TO DISCOVERY IF "LOWEST UNIT" RATE IS ADOPTED:**

1993	1994	1995	1996	4 YEAR TOTAL
\$13M	\$12M	\$11M	\$10M	\$46M

**ESTIMATED REVENUE LOSS TO TLC IF TIERING PRICES ARE CONSTRUED TO BE DISCRIMINATORY:**

1993	1994	1995	1996	4 YEAR TOTAL
\$0M	\$2M	\$5M	\$10M	\$17M

**TOTAL LOST REVENUE ESTIMATE:**

1993	1994	1995	1996	4 YEAR TOTAL
\$13M	\$14M	\$16M	\$20M	\$63M

# PROPOSED SOLUTIONS

## PROPOSED SOLUTIONS - PROGRAM ACCESS

- Presumption that pricing is not discriminatory or anti-competitive:
  - If programmer offers same rate card to alternate technologies (other than TVRO) as to cable affiliates
  - If rates to TVROs are under the average rate charged by non-vertically integrated programmers (less than 49¢)
- Create "safe harbor" for program services that serve 50% or more of SMATV, MMDC, TVRO and DBS (alternate technology) markets
- Grandfather existing contracts
- Create "safe harbor" for vertically integrated programmers whose practices closely parallel those of non-integrated programmers

# PROPOSED SOLUTIONS - RATE REGULATION

- ALLOW OPERATORS TO PASS THROUGH
  - NET CAPACITY EXPANSION COSTS
  - TECHNOLOGICAL IMPROVEMENT COSTS
  - PROGRAMMING COSTS

THESE PASS THROUGHS WILL ENCOURAGE INCREASED PROGRAMMING CHOICES FOR CONSUMERS & FOSTER NEW DEVELOPMENTS IN TECHNOLOGY WHICH WILL LEAD TO HIGHER QUALITY SERVICE. COST INCREASES WILL BE KEPT IN LINE BY EXTREMELY COMPETITIVE MARKET FORCES.

- REGULATE BASIC TIER BY SETTING PER CHANNEL RATE RATHER THAN OVERALL RATE.

OTHERWISE, OPERATORS WILL REMOVE NON MUST-CARRY SERVICES FROM BASIC. A PER CHANNEL RATE WILL DISCOURAGE TIERING AND THUS REDUCE THE LIKLIHOOD OF CONSUMER PRICE INCREASES

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## Fast Facts

7700 Wisconsin Avenue  
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DISCOVERY COMMUNICATIONS, INC.



# DISCOVERY COMMUNICATIONS, INC.

(continued)

## EXECUTIVE COMMITTEE:

John S. Hendricks  
*Founder, Chairman and CEO*  
*Discovery Communications, Inc.*

Ruth L. Otte  
*President and COO*  
*Discovery Networks*

Gregory B. Moyer  
*Executive Vice President*  
*Programming Group*

Greg Durig  
*Senior Vice President and*  
*Chief Financial Officer*

Domenick Fioravanti  
*Senior Vice President*  
*Corporate Development*  
*and International*

Bill McGowan  
*Senior Vice President*  
*Advertising Sales*

Judith A. McHale  
*Senior Vice President*  
*Corporate Services*  
*and General Counsel*

Chris Moseley  
*Senior Vice President*  
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# FAST FACTS

## The Discovery Channel Fast Facts

**Programming:** The Discovery Channel is the only cable network to feature 18 hours a day of the world's finest non-fiction entertainment covering nature and the environment, science and technology, history, adventure and the people who share our world.

**Hours:** 9 AM to 3 AM ET (18 hours per day)

**Launched:** June 17, 1985

**Affiliates:** 9,731 cable systems in all 211 DMA's

**Subscribers:** 59.4 million (A.C. Nielsen as of March 1993)

**Satellites:** Satcom C-4, transponder 21 (East Coast)  
Galaxy 5, transponder 12 (West Coast)

**Ownership:** Cox Cable Communications; John S. Hendricks; NewChannels Corp.; and TCI Development Corp.

**Executives:** John Hendricks  
Founder, Chairman and CEO  
Discovery Communications, Inc.

Ruth Otte  
President and Chief Operating Officer  
Discovery Networks

# The Discovery Channel

(continued)

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Dawn McCall  
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# FAST FACTS

## THE LEARNING CHANNEL

*The Learning Channel (TLC)* is the only cable network that consistently offers people of all ages -- from pre-schoolers on -- an enjoyable, entertaining way to learn and satisfy their natural curiosity. Relaunched October 1, 1991, this new *viewer friendly* service features stimulating, provocative non-fiction that awakens the power of the mind. *TLC* signature series and specials explore the humanities, arts, sciences, entertainment and much more that enriches and delights.

**PARENT COMPANY:** Discovery Communications, Inc.

**LAUNCH DATE:** November 1980  
(Acquired by Discovery Communications in May 1991)

**RE-LAUNCH:** October 1, 1991

**AFFILIATES:** 1522 cable systems in top 100 DMA's

**SATELLITE:** Satcom C-3, transponder 2

**SUBSCRIBERS:** 19.5 million households  
(Nielsen Universe Estimate, March 1993)  
Does not include alternate technologies distribution.

**EXECUTIVES:** John Hendricks  
*Founder, Chairman and CEO*  
*Discovery Communications, Inc.*

Ruth Otte  
*President and COO*  
*Discovery Networks*



-more-

# THE LEARNING CHANNEL

(continued)

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# FAST FACTS

## HISTORICAL HIGHLIGHTS

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### 1985

June 17

With financial backing from New York Life Insurance, Allen and Company Inc., and Group W Satellite Communications, The Discovery Channel, headed by founder, Chairman and CEO John Hendricks, launches on Galaxy 1 satellite, transponder 22, with approximately 156,000 subscribers.

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### 1986

June

Four multiple system cable operators (MSOs) join previous backers in making an investment in The Discovery Channel. They are: United Cable Television Corp., Cox Cable Communications, Inc., Newhouse Broadcasting Corp., and Tele-Communications Inc. (TCI).

June 17

Discovery marks first anniversary, serving seven million subscribers.

July

Discovery offers the cable industry's first rebate affiliate program allowing operators to receive rebates on their sub fees, based upon advertising sales revenues.

October

Former MTV Networks VP of Marketing, Ruth Otte, is named President and Chief Operating Officer of Discovery.

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### 1987

January

Discovery expands its programming schedule from 12 to 18 hours daily.

-Continued

February	Discovery, in association with Orbita Technologies Corporation, makes television history by broadcasting 66 hours of live Soviet television. <b>Russia: Live From the Inside</b> gives Americans their first glimpse of domestic Soviet television.
June 17	Discovery celebrates its second birthday announcing an unprecedented growth of 8.4 million subscribers for the first quarter of 1987, bringing subscriber base to 18.4 million (more than 100% growth over the previous year).
July	A.C. Nielsen begins to measure Discovery.
December	Discovery enters agreement with Mitsubishi Corporation which allows the latter to telecast Discovery programming in Japan via cable television and closed-circuit TV.  Discovery ends the year with 27.5 million subscribers, representing a 170% growth over the previous year.

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## 1988

January	Discovery is named the 1987 Golden ACE Award Winner for <b>Russia: Live From the Inside</b> .
April	Discovery is named the fastest growing cable television network in history by A.C. Nielsen.
June 17	Discovery celebrates its third anniversary with 32.1 million subscribers.
December	Discovery finishes the year with 38.1 million subscribers.

-Continued